Supreme Court, U.S.
FILED
DEC 3 2002
OFFICE OF THE CLERK

No. 02-320

IN THE

Supreme Court of the United States

DEMETRIOS KARAMANOS AND RICHARD PEDRONI,
Petitioners,

v.

UNITED STATES OF AMERICA

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

REPLY MEMORANDUM FOR THE PETITIONERS

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REPLY MEMORANDUM FOR THE PETITIONERS

1. In opposing certiorari, the government first contends (Br. in Opp. at 7, 14-15) that this federal prosecution was not for a state tax law offense but rather was directed solely against the use of the interstate wires, in violation of 18 U.S.C. 1343. The realities of the prosecution are precisely to the contrary. The alleged scheme to defraud the State of New Jersey of its excise taxes and gross receipts taxes was the heart of the allegations in the indictment relating to the wire fraud.[1] The use of the wires were incidental to the scheme. The court below informed the jury that if the "use of the wires can be reasonably foreseeable even though not actually

[1] The scheme to defraud as described in ¶¶ 1 to 37 of the Indictment at A237 to 45 and ¶¶ 4 to 30 at A248 to 58 were the basis of each wire fraud charge which incorporated them by reference. Each wire fraud charge identified its objective as obtaining the New Jersey excise taxes and gross receipts taxes. (E.g. A278).

intended" and if it was "reasonably foreseeable that wires would be used in the normal course of business," this element was satisfied. (A662-63)

The decision below cannot be reconciled with the Court's unanimous ruling in *Cleveland v. United States*, 531 U.S. 12 (2000), where the mails were used to send false state casino license applications. As the Court stated, in terms that speak directly to this case (531 U.S. at 24-25):

> We reject the Government's theories of property rights not simply because they stray from traditional concepts of property. We resist the Government's reading of § 1341 as well because it invites us to approve a sweeping expansion of federal criminal jurisdiction in the absence of a clear statement by Congress. Equating issuance of licenses or permits with deprivation of property would subject to federal mail fraud prosecution a wide range of conduct traditionally regulated by state and local authorities. We note in this regard that Louisiana's video poker statute typically and unambiguously imposes criminal penalties for making false statements on license applications [citation omitted]. As we reiterated last Term, "'unless Congress conveys its purpose clearly, it will not be deemed to have significantly changed the federal state balance' in the prosecution of crimes." *Jones v. United States*, 529 U.S. 848, 858 (2000) (quoting *United States v. Bass*, 404 U.S. 336, 349 (1971)).

The foregoing rationale proceeds upon the foundation previously established by *McNally v. United States*, 483 U.S. 350 (1987). There, the Court held that the mail fraud statute does not reach "schemes to defraud citizens of their intangible rights to honest and impartial government" (*id.* at 355) and that the statute is "limited in scope to the protection of property rights" (*id.* at 360). *See Carpenter v. United States*, 484 U.S. 19, 25 (1987). In response to this ruling,

Congress amended the mail fraud statute the following year to encompass "the intangible right of honest services." 18 U.S.C. 1346. Thus, in so doing, Congress clearly stated its purpose to exercise its constitutional authority and alter the federal-state balance in that specified area.[2]

Here, on the other hand, Congress has never expressed any intention to prosecute violations of state tax laws and thereby "place under federal superintendence a vast array of conduct traditionally policed by the States." *Cleveland v. United States*, *supra*, 531 U.S. at 27. Hence, just as the mailing of the false application for a State video poker license did not implicate the federal mail fraud statute in *Cleveland*, so too Petitioners' use of the wires did not justify their federal prosecution for conspiracy to evade purely local state excise taxes. The federal arrogation of state prosecutorial authority in this case is therefore precisely identical to the mail fraud prosecution at issue in *Cleveland*.[3] There is accordingly a

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[2] *United States v. Panarella*, 277 F.3d 678 (3d Cir. 2002), upon which the government relies (Br. in Opp. at 8-9), is distinguishable. There, the court upheld a federal wire fraud conviction of a Pennsylvania state senator for depriving the public of his "honest services" as a legislator for concealing a conflict of interest. *See* 18 U.S.C. 1343, 1346. In so holding, the court was "mindful that the prosecution of state public officials raises federalism concerns about the appropriateness of the federal government's interference with the operation of state and local governments" (*id.* at 693). The court concluded that the case fell within the terms of 18 U.S.C. 1346, the post-*McNally* amendment of the wire fraud statute. Here, however, there is no comparable statutory amendment that would include state tax offenses within the wire fraud statute.

[3] Absent a clear statement by Congress to include state tax law offenses in the federal wire fraud statute (18 U.S.C. 1346), it should "not be deemed to have significantly changed the federal-state balance." *United States v. Bass*, 404 U.S. 336, 349 (1971). Contrary to the government's argument, (Br. in Opp. at 12, n. 3), the canon of constitutional doubt is therefore fully applicable in this case involving asserted federal criminalization of conduct that is one of traditional state concern. *See, e.g., Jones v. United States*, 529 U.S. 848 (2000).

conflict between the decision below and *Cleveland*, which requires resolution by this Court.

The government suggests that the award of *all* of the restitution and fines to the federal government, and none to the State was somehow warranted by the form of the conspiracy charge. (Br. in Opp. at 9, n.2) The conspiracy alleged involved the evasion of state taxes (excise and gross receipts) and federal excise taxes that were roughly equivalent on a per gallon basis. (A237 and A239). But despite the fact that Pedroni was acquitted of all substantive charges that he violated any *federal* excise tax laws, the federal court nevertheless awarded 100% of the $500,000 restitution levied against him to the federal government. This fact dramatically illustrates the federal transformation, indeed usurpation, of the State's prerogatives to enforce its own tax code in accordance with its terms. Moreover, the disparity worked by the length of the period of incarceration for the federal offense likewise demonstrates the onerous consequence of the federal criminalization of what was a State offense. Transforming the term of imprisonment so dramatically also highlights this interference. (Pet. 11-12 and n.4).[4]

2. Contrary to the government's assertion (Br. in Opp. at 12-14), Petitioners' federalism claim involves questions upon which the circuits are divided in *United States v. Boots*, 80 F.3d 580 (1st Cir.), *cert. denied*, 519 U.S. 905 (1996); *United States v. Pasquantino*, 305 F.3d 291 (4th Cir. 2002); and *United States v. Trapilo*, 130 F.3d 547 (2d Cir. 1997), *cert. denied*, 525 U.S. 812 (1998). In those cases, the First and

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[4] The government flatly asserts (Br. in Opp. at 8) that New Jersey's right to prosecute is unaffected by the federal prosecution. That is not correct. New Jersey has a broad statute expanding on its own constitution's double jeopardy protections. Under N.J.S.A. § 2C:1-10, it appears that the State prosecution may be precluded by the federal prosecution.

Fourth Circuits, invoking the common law revenue rule, have held that the federal wire fraud statute cannot reach a scheme to defraud a foreign government of tax revenue. The Second Circuit has ruled to the contrary.

The government seeks to confine the scope of this conflict to the application of the revenue rule to tax offenses against foreign governments. (Br. in Opp. at 12) But the decisions of this Court, from the earliest days of the Republic, have equated the tax claims of foreign sovereigns with tax claims of the sovereign States of the Union. Thus, Chief Justice Marshall declared in *The Antelope*, 23 U.S. (10 Wheat 66), 123 (1825) that "the courts of no country execute the penal laws of another." From this premise, this Court held a half century later that Marshall's dictum applied not only to criminal prosecutions, but "to all suits for the recovery of pecuniary penalties for any violation of statutes for protection of its revenue . . . ." *Wisconsin v. Pelican Insurance Co. of New Orleans*, 127 U.S. 265, 290 (1887). In that case, the Court rejected a claim by Wisconsin for tax penalties assessed against an out-of-state corporation. For these purposes, Wisconsin was treated as a foreign country *vis-a-vis* the out-of-state taxpayer. The Court applied the revenue rule equally to state and foreign sovereigns' efforts to enforce tax penalties in federal courts. The Court observed that:

> The rule that the courts of no country execute the penal law of another applies not only to *prosecutions and sentences for crimes and misdemeanors, but to all suits in favor of the state for the recovery of pecuniary penalties for any violation of statutes for protection of its revenue, or other municipal laws and to all judgments for such penalties*.... (emphasis added) [5]

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[5] Subsequently, the Court clarified that a state tax judgment rendered in the courts of one state can be enforced in the federal or state courts of another state in accordance with the Full Faith and Credit Clause. *Milwaukee County v. M.E. White Co.*, 296 U.S. 268, 275 (1935).

The foregoing analysis was subsequently applied in *Moore v. Mitchell*, 30 F.2d 600 (2d Cir. 1929), *aff'd*, 281 U.S. 18 (1930). There, the court dismissed a suit by Indiana brought in the federal court in New York for delinquent taxes on the authority of *Pelican Insurance Co. supra.* In a concurring opinion, Judge Learned Hand reaffirmed the equivalence between criminal sanctions and tax liabilities, observing that "[r]evenue laws fall within the same reasoning; they affect a state in matters as vital to existence as its criminal laws" (30 F.2d at 604). Thus, this federal prosecution for conspiracy to evade New Jersey excise taxes seeks to enforce criminal sanctions with respect to two matters—taxes and crimes—that are exclusively rooted in New Jersey's sovereign existence. Accordingly, absent a clear statement by Congress, such offenses should only be prosecuted by the State of New Jersey in the New Jersey courts.[6]

Like the revenue rule dealing with foreign countries, the Tenth Amendment treats the states as independent sovereign entities which are exclusively responsible to enforce their own criminal laws and their own revenue laws. The decision below upholding Petitioners' convictions to commit state tax offenses countenances an unwarranted expansion of federal authority into both state criminal law and state tax enforcement that departs from the federal-state balance prescribed by the Constitution. Review by this Court is therefore justified.

3. Finally, the government notes that "[e]very court of appeals that has considered the question has concluded that mail and wire fraud statute encompass scheme to defraud a state of tax revenues" (Br. in Opp. at 14.) The existence of such authority makes the need for this Court's review even more compelling. For absent plenary consideration by the

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[6] This Court affirmed in *Moore* on the ground that the Indiana tax officials lacked authority to bring the suit in federal court.

Court, the Justice Department and each of its United States Attorneys' Offices located in every State will continue to prosecute such cases in derogation of the federalism standards established in *Lopez*, *Morrison*, and *Cleveland*.[7]

Most importantly, all of the authorities cited by the government [8] in support of its argument antedate this Court's seminal decisions redefining the scope of the authority of the National Government in our federal system and the reach of the mail and wire fraud statutes. *Boots*, which rejects federal criminalization, and *Pasquantino*, were decided after *Lopez* and both reject the federal criminalization of other jurisdictions' tax offenses. In *Lopez*, the Court invalidated a federal criminal statute prohibiting the knowing possession of

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[7] *Lopez* and *Morrison* cannot be distinguished, as the government asserts (Br. in Opp. at 10-12), on the ground that they did not involve the use of the channels or instrumentalities of interstate commerce. Those decisions provide the fundamental doctrinal framework for the Court's recognition that the States' power to enforce its criminal laws is primary and paramount. As we have pointed out (Pet. 14, n. 3), the fact that Congress may constitutionally regulate the channels or instrumentalities of interstate commerce does not address the critical question that *McNally* and *Cleveland* require to be answered here, *viz.*, whether Congress clearly intended the federal wire fraud statute (18 U.S.C. 1343) to authorize federal prosecutions of state and local tax violations. In light of *McNally* and *Cleveland*, there is no merit in the government's reliance (Br. in Opp. at 7-8) upon older *dicta* suggesting that the mail and wire fraud statutes encompass any conduct that is "contrary to public policy" or conduct that is prohibited under "other laws." Cf. *Parr v. United States*, 363 U.S. 370, 389 (1960), quoting *Badders v. United States*, 240 U.S. 391, 393 (1916).

[8] *See, e.g.*, *United States v. DeFiore*, 720 F.2d 757, 761 (2d Cir. 1983), *cert. denied*, 466 U.S. 906 (1984); *United States v. Mirabile*, 503 F.2d 1065, 1066-1067 (8th Cir. 1974), *cert. denied*, 420 U.S. 973 (1975); *United States v. Helmsley*, 941 F.2d 71, 94 (2d Cir. 1991); *cert. denied*, 502 U.S. 1091 (1992); *United States v. Bucey*, 876 F.2d 1297, 1309 (7th Cir.), *cert. denied*, 493 U.S. 1004 (1989); *United States v. Doe*, 867 F.2d 986, 989 (7th Cir. 1989); *United States v. Porcelli*, 865 F.2d 1352, 1359-1361 (2d Cir.), *cert. denied*, 493 U.S. 810 (1989).

a firearm in a school zone. In the Court's view, the federal criminalization of such local conduct that is already denounced by state law "effects a 'change in the sensitive relation between federal and state criminal jurisdiction.' [citation omitted]" (514 U.S. at 561, n. 3). Accord: *United States v. Morrison*, 529 U.S. 598 (2000). In these rulings, the Court made clear that "The Constitution requires a distinction between what is truly national and what is truly local." (529 U.S. at 617-618). Since nothing can be more truly local than state, county or municipal revenue laws, review by this Court is amply warranted.

CONCLUSION

For the reasons stated above and in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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December 3, 2002